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RUEHMO/AMEMBASSY MOSCOW 0069
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C O N F I D E N T I A L SECTION 01 OF 03 MAPUTO 001073

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TAGS: ENRG EPET EMIN EINV ETRD SENV MZ SF
SUBJECT: HYDROCARBONS IN MOZAMBIQUE: UNTAPPED POTENTIAL

REF: A. MAPUTO 1051
¶B. MAPUTO 1018
¶C. MAPUTO 972
¶D. 07 ALGIERS 1694

Classified By: Classified By: Charge d'Affaires Todd C. Chapman, Reason s 1.4(b+d)

¶1. (U) This cable represents the third in a series in an innovative collaboration in energy/resource reporting and commercial advocacy between Embassies Maputo and Pretoria. Embassy Pretoria Minerals/Energy Officer and Maputo Political/Economic officer visited energy/minerals projects in northern Tete province and met relevant government and private officials in Maputo October 13-17, 2008.

¶2. (C) Summary: Embassy Maputo and Pretoria officers met with Mozambican government and private energy company officials regarding oil and gas exploration and development in Mozambique. To date, exploration drilling has been sparse and concentrated in the Mozambique Basin, though Mozambican and Anadarko Petroleum officials were optimistic about the possibility of liquid hydrocarbons in northern Mozambique's Rovuma basin. Anadarko described the logistic and cost challenges associated with exploring in remote northern Mozambique and complained of the GRM's plans to impose foreign exchange controls and enforce stringent domestic labor requirements, opining that these could slow oil and gas development in Mozambique. Southern African countries could tap marginal gas finds for local gas-fired power generation, though the region's poor power regulatory regimes made Anadarko pessimistic about potential gas-to-power schemes. Mozambique's hydrocarbon exploration future most likely hinges on firms discovering oil rather than gas, and the industry will watch early movers closely.

HYDROCARBON SECTOR OVERVIEW

¶3. (SBU) Emboffs met with Mozambican National Petroleum Institute (INP) Exploration Manager Carlos Zacarias and Anadarko Petroleum's country managing director John Peffer to discuss Mozambique's hydrocarbon prospects. The INP is

aggressively pursuing foreign firms, either by direct negotiation or by bid round, to invest in its coastal exploration blocks and build upon the modest successes of the Pande-Temane onshore gas fields. Foreign firms since the 1950s have been acquiring seismic and drilling exploration wells in Mozambique's coastal regions, both onshore and offshore, and have identified the Mozambique Basin and Rovuma Basin as the country's most prospective for hydrocarbons.

¶4. (SBU) To date, exploration drilling has been sparse and concentrated exclusively in the Mozambique Basin. Firms have drilled about 100 exploration wells in Mozambique and commercial finds remain small and limited to natural gas or condensate. South Africa's Sasol started production from the Temane gas field in 2004 and together with the addition of the Pande and Inhassoro condensate fields in 2008 and 2011 respectively, the $1.2 billion project will supply 490 million cubic feet per day (mmcfd) of gas by the middle of the next decade to industrial and commercial customers in South Africa by way of an 865 kilometer pipeline to Secunda, according to a respected UK-based oil industry consultancy. Zacarias mentioned that Sasol had plans to boost the pipeline's current capacity by 40 percent to accommodate these additional fields and had recently begun exploration drilling in blocks 16 and 19.

ANADARKO OPENS UP ROVUMA BASIN

¶5. (SBU) Zacarias and Peffer separately shared details of

Anadarko's aggressive plans for seven offshore exploration wells (4 deepwater and 3 on the narrow continental shelf) in previously undrilled northern Mozambique's Rovuma Basin Areas 1 and 4 at a cost of $30 to $40 million per well. Anadarko on January 1, 2009 also will take over operatorship of the onshore Rovuma block from its Canadian partner Artumas, who operates the offshore Mnazi Bay project on the other side of the Tanzanian border. Peffer told Emboffs that Anadarko during the first half of 2008 had shot 3300 square kilometers of 3D seismic in the deepwater region that suggested Tertiary fluvial fans and toe thrusts geologically similar to West Africa and the Gulf of Mexico and planned to shoot 2D seismic in the shallow water region in 2009. Anadarko anticipates a five year exploration program and expects to drill its first deepwater well in late 2009 using internally-supplied rigs and to contract available jackup rigs from the Middle East to begin drilling in the shallow water in 2010 or 2011.

¶6. (SBU) Peffer conceded that exploration to date suggests that Southern Africa is gas-proned, but he was optimistic that Anadarko would find oil in the deepwater. Zacarias assessed that the region's hydrocarbons became "wetter8 as one moved offshore, suggesting a greater prevalence of liquid hydrocarbons offshore. Northern Mozambique's remoteness from major logistical hubs, however, makes exploration in the Rovuma Basin extremely costly because of an inability to share scale economies with other operators; Anadarko purpose-built its Pemba operating base for its drilling campaign. Furthermore, local political pressure for Anadarko to invest in local economic development and use local labor precluded it from taking advantage of other ports in Kenya or Tanzania; Anadarko's onshore seismic program was the most expensive per kilometer of seismic that Peffer had ever seen.

FISCAL AND LABOR POLICIES ARE WORRISOME

¶7. (C) Peffer identified two policy trends that he believed could threaten future oil and gas exploration in Mozambique. First, he believed that Maputo's plans to impose foreign exchange controls, ostensibly to bolster the GRM's

balance of payments, threatened oil firms, ability to repatriate profits. Anadarko supposedly enjoys grandfathered status with regards to this regulation, but fears that future concessionaires may have reservations if the controls are enacted. (Note: Anadarko has experienced similar problems in other countries and Peffer specifically cited Algeria and Venezuela as examples. According to US Embassy Algiers (reftel), Algeria in 2007 backtracked on its hydrocarbon sector liberalization, instituting a windfall profits tax. Anadarko is Algeria's chief foreign oil producer and is currently engaged in arbitration with Sonatrach over the tax. End Note).

¶8. (SBU) Second, Mozambique's onerous local content requirements also pose problems for foreign operators because Mozambican labor lacks the technical skills that the industry requires. The Labor Minister told Peffer that she was aware of the issue and advised that the GRM may consider granting the minerals industry special consideration on the local content requirement. Peffer observed however, that it was a public secret that Sasol enjoyed a "different8 relationship with the GRM and did not face such stringent requirements.

GAS-TO-POWER "WON'T HAPPEN8

¶9. (SBU) When asked about the possibility of Mozambique or its neighbors tapping sub-commercial gas finds for gas-to-power schemes as Tanzania has done with its Songo Songo project, Peffer suggested that Mozambique could support a 500MW power plant with domestically-produced gas, but that

gas-to-power in Southern Africa was a "complicated mess8 and that such projects "won't happen.8 Poorly developed local electricity regulatory systems leave oil firms to negotiate power offtake down to the end user, which complicates project contracts and financing. Peffer said that oil firms had no patience with power purchase issues, but probably would consider additional East African gas-to-power projects if states would guarantee payment for the offtake from privately operated plants.

COMMENT: OPTIMISM ABOUT POTENTIAL OIL AND GAS

¶10. (C) Maputo is optimistic about the possibility of new oil and gas finds, but gas-proned Southern Africa's lack of infrastructure and few major commercial finds are likely to make it difficult for firms to justify world-scale gas export projects such as liquefied natural gas (LNG) or gas-to-liquids (GTL). Cost overruns from materials and engineering, as with Qatar's Pearl LNG project, make these gas projects difficult to bank even under the best of circumstances. Mozambique's hydrocarbon exploration future most likely hinges on firms discovering oil rather than gas, and the industry will watch early movers such as Sasol and Anadarko. Southern Africa's remoteness from major exploration hotbeds such as West Africa and the Gulf of Mexico discourages firms from exploring on-the-margin due to scarcity of nearby offshore drill rigs and the extreme cost of moving offshore rigs between regions. (Note: According to Peffer it costs about $40 million to move one offshore rig from Brazil to East Africa). As evidenced by Woodside's $100 million duster offshore Kenya, a series of multi-million dollar dry holes would be a catastrophic setback for hydrocarbons exploration in Mozambique. While Mozambique could potentially become another negative example of an oil-rich African economy, the country's historic ties with Norwegian consultants and its willingness to join the Extractive Industries Transparency Initiative (EITI) later this year, suggests that Mozambique may be serious about transparent management of oil resources should they become a reality.